

ASSEMBLY BILL

No. 2111

Introduced by Assembly Member Smyth

February 18, 2010

An act to amend Sections 9855, 9855.2, and 9855.9 of the Business and Professions Code, to amend Section 1794.41 of the Civil Code, and to amend Sections 12800 and 12830 of, and to repeal Section 116.5 of, the Insurance Code, relating to service contracts.

LEGISLATIVE COUNSEL'S DIGEST

AB 2111, as introduced, Smyth. Service contracts.

(1) Existing law regulates service contracts, as defined, relating to maintenance or repair of specified sets and appliances. A service contract may include provisions for incidental payment of indemnity, not exceeding the retail value of \$250 per year. Existing law prohibits a service contract administrator, as defined, from being an obligor on a service contract.

This bill would change the definition of service contract by expanding the items a contract may cover to include accessories of electronic sets or appliances. The bill would delete the \$250 per year limit on incidental payments. The bill would also change the definition of service contract administrator to no longer exclude service contract sellers and insurers admitted to do business in the state. The bill would authorize a service contract administrator to be an obligor on a service contract where all service contracts under which the service contract administrator is obligated to perform are insured under a service contract reimbursement insurance policy.

The bill would make other technical and clarifying changes.

(2) Existing law prohibits a service contract seller from issuing a service contract without complying with specific requirements. The provisions regarding service contracts are in effect until January 1, 2013.

This bill would instead prohibit a service contract seller from issuing a service contract unless the obligor under the contract has complied with specific requirements. The bill would extend the repeal date for the provisions regarding service contracts to January 1, 2018.

(3) Existing law prohibits a service contract covering any motor vehicle, home appliance, or home electronic product purchased for use in this state from being offered for sale or sold unless several elements exist, including that the contract is cancelable by the purchaser under certain conditions.

This bill would change the required conditions of a cancellation in that the seller would no longer be required to indicate in the contract which of specified bases for a pro rata refund the seller is using.

(4) Existing law provides that an express warranty warranting a motor vehicle lubricant, treatment, fluid, or additive that covers incidental or consequential damage resulting from a failure of the lubricant, treatment, fluid, or additive, is automobile insurance, unless certain requirements are met.

This bill would delete those provisions.

(5) Existing law defines vehicle service contract for purposes of provisions relating to sellers of vehicles.

This bill would add to the definition of a vehicle service contract an agreement, provided with or without separate consideration, that promises to repair, replace, or maintain a motor vehicle or watercraft, or to indemnify for the repair, replacement, or maintenance of a motor vehicle or watercraft, conditioned upon the use of a specific brand or brands of lubricant, treatment, fluid, or additive.

(6) Existing law requires that prior to incurring an obligation under a vehicle service contract, an obligor file with the Insurance Commissioner, and receive the commissioner's approval to use, a copy of an insurance policy covering 100% of the obligor's vehicle service contract obligations. An obligor is authorized to have on file with the commissioner only one active policy from one insurer at any time. Any violation of this provision is a crime.

This bill would authorize an obligor to have more than one policy on file with the commissioner where the obligor annually files with the commissioner a report certified as accurate by an officer or director of

the obligor that lists each of its insured vehicle service contract programs and the corresponding insurance policy under which each program is insured. Because this bill would create a new crime, it would impose a state-mandated local program.

(7) The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: yes.

The people of the State of California do enact as follows:

1 SECTION 1. Section 9855 of the Business and Professions
2 Code is amended to read:

3 9855. The definitions used in this section shall govern the
4 construction and terms as used in this chapter:

5 (a) ~~(1)~~—“Service contract” means a contract in writing to
6 perform, over a fixed period of time or for a specified duration,
7 services relating to the maintenance, replacement, or repair of
8 *an electronic* set or appliance, as defined by this chapter, *and their*
9 *accessories* or of furniture, jewelry, lawn and garden equipment,
10 power tools, fitness equipment, telephone equipment, small kitchen
11 appliances and tools, or home health care products, and may
12 include provisions for incidental payment of indemnity under
13 limited circumstances, including, but not limited to, power surges,
14 food spoilage, or accidental damage from handling.

15 ~~(2) Incidental payment of indemnity under paragraph (1) shall~~
16 ~~not exceed a retail value of two hundred fifty dollars (\$250) per~~
17 ~~year.~~

18 (b) “Service contract administrator” or “administrator” means
19 a person, ~~other than a service contract seller or an insurer admitted~~
20 ~~to do business in this state~~, who performs or arranges, or has an
21 affiliate who performs or arranges, the collection, maintenance,
22 or disbursement of moneys to compensate any party for claims or
23 repairs pursuant to a service contract, and who also performs or
24 arranges, or has an affiliate who performs or arranges, any of the
25 following activities on behalf of service contract sellers:

26 (1) Providing service contract sellers with service contract forms.

(2) Participating in the adjustment of claims arising from service contracts.

(3) Arranging on behalf of service contract sellers the insurance required by Section 9855.2.

A service contract administrator shall not be an obligor on a service contract *unless all service contracts under which the service contract administrator is obligated to perform are insured under a service contract reimbursement insurance policy.*

(c) (1) “Service contract seller” or “seller” means a person who sells or offers to sell a service contract to a service contractholder, including a person who is the obligor under a service contract sold by the seller, manufacturer, or repairer of the product covered by the service contract.

(2) “Service contract seller” or “seller” also includes a third party, including an obligor, who is not the seller, manufacturer, or repairer of the product.

(d) “Service contractholder” means a person who purchases or receives a service contract from a service contract seller.

(e) “Service contractor” means a service contract administrator or a service contract seller.

(f) “Service contract reimbursement insurance policy” means a policy of insurance issued by an insurer admitted to do business in this state providing coverage for all obligations and liabilities incurred by a service contract seller under the terms of the service contracts sold in this state by the service contract seller to a service contractholder. The service contract reimbursement insurance policy shall either cover all service contracts sold or specifically cover those contracts sold to residents of the State of California.

(g) “Obligor” is the entity financially and legally obligated under the terms of a service contract.

(h) The terms “consumer goods,” “manufacturer,” “retail seller,” “retailer,” and “sale” shall have the same meanings ascribed to them in Section 1791 of the Civil Code.

SEC. 2. Section 9855.2 of the Business and Professions Code is amended to read:

9855.2. (a) A service contract seller shall not issue, sell, or offer for sale a service contract ~~unless he or she complies the~~ *obligor under the service contract has complied* with one of the following requirements:

(1) Files with the director one of the following:

1 (A) The most recent annual report on Form 10-K required by
2 the Securities and Exchange Commission, reflecting a net worth
3 greater than the sum of the deferred revenues from service contracts
4 in force. If the service contractor is a foreign corporation that files
5 a comparable audited financial statement with its home government
6 or with the United States government, the director may deem that
7 statement an acceptable substitute for Form 10-K.

8 (B) The most recent audited financial statement reflecting a net
9 worth of not less than one hundred million dollars (\$100,000,000).
10 The financial statement shall be certified by a certified public
11 accountant who is licensed in the state where the service contract
12 seller maintains its principal place of business or the seller's state
13 of domestic incorporation.

14 (2) Obtains a service contract reimbursement insurance policy.

15 (3) Sells service contracts that are administered by a service
16 contract administrator who has obtained a service contract
17 reimbursement insurance policy covering the seller's service
18 contracts.

19 (4) Maintains and annually verifies to the director a funded
20 account held in escrow equal to a minimum of 25 percent of the
21 deferred revenues from the service contracts in force.

22 (b) A service contract administrator shall not administer service
23 contracts sold in this state unless a service contract reimbursement
24 insurance policy covering these service contracts has been obtained.

25 SEC. 3. Section 9855.9 of the Business and Professions Code
26 is amended to read:

27 9855.9. This article shall remain in effect only until January
28 1, ~~2013~~, 2018, and as of that date is repealed, unless a later enacted
29 statute, that is enacted before January 1, ~~2013~~, 2018, deletes or
30 extends that date.

31 SEC. 4. Section 1794.41 of the Civil Code is amended to read:

32 1794.41. (a) No service contract covering any motor vehicle,
33 home appliance or home electronic product purchased for use in
34 this state may be offered for sale or sold unless all of the following
35 elements exist:

36 (1) The contract shall contain the disclosures specified in Section
37 1794.4 and shall disclose in the manner described in that section
38 the buyer's cancellation and refund rights provided by this section.

39 (2) The contract shall be available for inspection by the buyer
40 prior to purchase and either the contract, or a brochure which

1 specifically describes the terms, conditions, and exclusions of the
2 contract, and the provisions of this section relating to contract
3 delivery, cancellation, and refund, shall be delivered to the buyer
4 at or before the time of purchase of the contract. Within 60 days
5 after the date of purchase, the contract itself shall be delivered to
6 the buyer. If a service contract for a home appliance or a home
7 electronic product is sold by means of a telephone solicitation, the
8 seller may elect to satisfy the requirements of this paragraph by
9 mailing or delivering the contract to the buyer not later than 30
10 days after the date of the sale of the contract.

11 (3) The contract is applicable only to items, costs, and time
12 periods not covered by the express warranty. However, a service
13 contract may run concurrently with or overlap an express warranty
14 if (A) the contract covers items or costs not covered by the express
15 warranty or (B) the contract provides relief to the purchaser not
16 available under the express warranty, such as automatic
17 replacement of a product where the express warranty only provides
18 for repair.

19 (4) The contract shall be cancelable by the purchaser under the
20 following conditions:

21 (A) Unless the contract provides for a longer period, within the
22 first 60 days after receipt of the contract, or with respect to a
23 contract covering a used motor vehicle without manufacturer
24 warranties, a home appliance, or a home electronic product, within
25 the first 30 days after receipt of the contract, the full amount paid
26 shall be refunded by the seller to the purchaser if the purchaser
27 provides a written notice of cancellation to the person specified in
28 the contract, and if no claims have been made against the contract.
29 If a claim has been made against the contract either within the first
30 60 days after receipt of the contract, or with respect to a used motor
31 vehicle without manufacturer warranties, home appliance, or home
32 electronic product, within the first 30 days after receipt of the
33 contract, a pro rata refund, based on either elapsed time or an
34 objective measure of use, such as mileage or the retail value of
35 any service performed, at the seller's option ~~as indicated in the~~
36 ~~contract~~, shall be made by the seller to the purchaser if the
37 purchaser provides a written notice of cancellation to the person
38 specified in the contract.

39 (B) Unless the contract provides for a longer period for obtaining
40 a full refund, after the first 60 days after receipt of the contract, or

with respect to a contract covering a used motor vehicle without manufacturer warranties, a home appliance, or a home electronic product, after the first 30 days after the receipt of the contract, a pro rata refund, based on either elapsed time or an objective measure of use, such as mileage or the retail value of any service performed, at the seller's option ~~as indicated in the contract~~, shall be made by the seller to the purchaser if the purchaser provides a written notice of cancellation to the person specified in the contract. In addition, the seller may assess a cancellation or administrative fee, not to exceed 10 percent of the price of the service contract or twenty-five dollars (\$25), whichever is less.

(C) If the purchase of the service contract was financed, the seller may make the refund payable to the purchaser, the assignee, or lender of record, or both.

(b) Nothing in this section shall apply to a home protection plan that is issued by a home protection company which is subject to Part 7 (commencing with Section 12740) of Division 2 of the Insurance Code.

~~(e) The amendments to this section made at the 1988 portion of the 1987-88 Regular Session of the Legislature that extend the application of this section to service contracts on home appliances and home electronic products shall become operative on July 1, 1989.~~

~~(d)~~
(c) If any provision of this section conflicts with any provision of Part 8 (commencing with Section 12800) of Division 2 of the Insurance Code, the provision of the Insurance Code shall apply instead of this section.

SEC. 5. Section 116.5 of the Insurance Code is repealed.

~~116.5.—An express warranty warranting a motor vehicle lubricant, treatment, fluid, or additive that covers incidental or consequential damage resulting from a failure of the lubricant, treatment, fluid, or additive, shall constitute automobile insurance, unless all of the following requirements are met:~~

~~(a) The obligor is the primary manufacturer of the product. For the purpose of this section, "manufacturer" means a person who can prove clearly and convincingly that the per unit cost of owned or leased capital goods, including the factory, used to produce the product, plus the per unit cost of nonsubcontracted labor used to produce the product, exceeds twice the per unit cost of raw~~

1 materials used to produce the product. “Manufacturer” also means
2 a person who has formulated or produced, and continuously offered
3 in this state for more than nine years, a motor vehicle lubricant,
4 treatment, fluid, or additive.

5 (b) ~~The commissioner has issued a written determination that~~
6 ~~the obligor is a manufacturer as defined in subdivision (a). An~~
7 ~~obligor shall provide the commissioner with all information,~~
8 ~~documents, and affidavits reasonably necessary for this~~
9 ~~determination to be made. Approval by the commissioner shall be~~
10 ~~obtained prior to January 1, 2004, or prior to the issuance of a~~
11 ~~warranty subject to this section, whichever is later. If the~~
12 ~~commissioner determines that the obligor is not a manufacturer,~~
13 ~~the obligor may obtain a hearing in accordance with Chapter 4.5~~
14 ~~(commencing with Section 11400) of Part 1 of Division 3 of Title~~
15 ~~2 of the Government Code.~~

16 (c) ~~The agreement covers only damage incurred while the~~
17 ~~product was in the vehicle.~~

18 (d) ~~The agreement is provided automatically with the product~~
19 ~~at no extra charge.~~

20 SEC. 6. Section 12800 of the Insurance Code is amended to
21 read:

22 12800. The following definitions apply for purposes of this
23 part:

24 (a) “Motor vehicle” means a self-propelled device operated
25 solely or primarily upon land and may include both self-propelled
26 motor homes or recreational vehicles, non-self-propelled camping
27 and recreational trailers, off-road vehicles, and trailers designed
28 to transport off-road vehicles. However, “motor vehicle” shall not
29 include a self-propelled vehicle, or a component part of such a
30 vehicle, that has any of the following characteristics:

31 (1) Has a gross vehicle weight rating of 30,000 pounds or more,
32 and is not a recreational vehicle as defined by Section 18010 of
33 the Health and Safety Code.

34 (2) Is designed to transport more than 15 passengers, including
35 the driver.

36 (3) Is used in the transportation of materials considered
37 hazardous pursuant to the Hazardous Materials Transportation Act
38 (49 U.S.C. Sec. 5101 et seq.), as amended.

39 (b) “Watercraft” means a vessel, as defined in Section 21 of the
40 Harbors and Navigation Code, and may include any

1 non-self-propelled trailer used to transport such watercraft upon
2 land.

3 (c) (1) “Vehicle service contract” means a contract or agreement
4 for a separately stated consideration and for a specific duration to
5 repair, replace, or maintain a motor vehicle or watercraft, or to
6 indemnify for the repair, replacement, or maintenance of a motor
7 vehicle or watercraft, necessitated by an operational or structural
8 failure due to a defect in materials or workmanship, or due to
9 normal wear and tear.

10 (2) A vehicle service contract may also provide for the incidental
11 payment of indemnity under limited circumstances only in the
12 form of the following additional benefits: coverage for towing,
13 substitute transportation, emergency road service, rental car
14 reimbursement, reimbursement of deductible amounts under a
15 manufacturer’s warranty, and reimbursement for travel, lodging,
16 or meals.

17 (3) “Vehicle service contract” also includes an agreement of a
18 term of at least one year, for separately stated consideration, that
19 promises routine maintenance.

20 (4) *“Vehicle service contract” also includes an agreement,*
21 *provided with or without separate consideration, that promises to*
22 *repair, replace, or maintain a motor vehicle or watercraft, or to*
23 *indemnify for the repair, replacement, or maintenance of a motor*
24 *vehicle or watercraft, conditioned upon the use of a specific brand*
25 *or brands of lubricant, treatment, fluid, or additive.*

26 ~~(4)~~

27 (5) Notwithstanding Section 116, and paragraphs (1) and (2) of
28 this subdivision, a vehicle service contract also includes one or
29 more of the following:

30 (A) An agreement that promises the repair or replacement of a
31 tire or wheel necessitated by wear and tear, defect, or damage
32 caused by a road hazard. However, an agreement that promises
33 the repair or replacement of a tire necessitated by wear and tear,
34 defect, or damage caused by a road hazard, in which the obligor
35 is the tire manufacturer, is exempt from the requirements of this
36 part. A warranty provided by a tire or wheel distributor or retailer
37 is exempt from the requirements of this part as long as the warranty
38 covers only defects in the material or workmanship of the tire or
39 wheel.

(B) An agreement that promises the repair or replacement of glass on a vehicle necessitated by wear and tear, defect, or damage caused by a road hazard. However, a warranty provided by a vehicle glass manufacturer is exempt from the requirements of this part. A warranty provided by a vehicle glass distributor or retailer is exempt from the requirements of this part as long as the warranty covers only defects in the material or workmanship of the vehicle glass.

(C) An agreement that promises the removal of a dent, ding, or crease without affecting the existing paint finish using paintless dent repair techniques, and which expressly excludes the replacement of vehicle body panels, sanding, bonding, or painting.

(d) “Service contract administrator” or “administrator” means any person, other than an obligor, who performs or arranges, directly or indirectly, the collection, maintenance, or disbursement of moneys to compensate any party for claims or repairs pursuant to a vehicle service contract, and who also performs or arranges, directly or indirectly, any of the following activities with respect to vehicle service contracts in which a seller located within this state is the obligor:

(1) Providing sellers with service contract forms.

(2) Participating in the adjustment of claims arising from service contracts.

(e) “Purchaser” means any person who purchases a vehicle service contract from a seller.

(f) “Seller” means either of the following:

(1) With respect to motor vehicles, a dealer or lessor-retailer licensed in one of those capacities by the Department of Motor Vehicles and who sells vehicle service contracts incidental to his or her business of selling or leasing motor vehicles.

(2) With respect to watercraft, a person who sells vehicle service contracts incidental to that person’s business of selling or leasing watercraft vehicles.

(g) “Obligor” means the entity legally obligated under the terms of a service contract.

SEC. 7. Section 12830 of the Insurance Code is amended to read:

12830. (a) Prior to incurring an obligation under a vehicle service contract, an obligor shall file with the commissioner, to the attention of the legal division, and receive the commissioner’s

1 approval to use, a copy of an insurance policy covering 100 percent
2 of the obligor's vehicle service contract obligations. The policy
3 must be issued by an insurer admitted in this state and authorized
4 by the commissioner to issue that insurance in this state. The policy
5 may also be issued by a risk retention group, as that term is defined
6 in 15 U.S.C. Sec. 3901(a)(4), as long as that risk retention group
7 is in full compliance with the federal Liability Risk Retention Act
8 of 1986 (15 U.S.C. Sec. 3901 and following), is in good standing
9 in its domiciliary jurisdiction, and has registered with the
10 commissioner pursuant to Chapter 1.5 (commencing with Section
11 125) of Part 1 of Division 1. The insurance required by this
12 subdivision shall be subject to the following:

13 (1) The insurer or risk retention group shall, at the time the
14 policy is filed with the commissioner, and continuously thereafter,
15 be rated "B++" or better by A. M. Best Company, Inc., maintain
16 surplus as to policyholders and paid-in capital of at least fifteen
17 million dollars (\$15,000,000), and annually file audited financial
18 statements with the commissioner.

19 (2) The commissioner may authorize an insurer or risk retention
20 group that has surplus as to policyholders and paid-in capital of
21 less than fifteen million dollars (\$15,000,000) but at least equal to
22 ten million dollars (\$10,000,000) to issue the insurance required
23 by this paragraph if the insurer or risk retention group demonstrates
24 to the satisfaction of the commissioner that the company maintains
25 a ratio of direct written premiums, wherever written, to surplus as
26 to policyholders and paid-in capital of not more than 3 to 1.

27 (3) An obligor required to maintain insurance pursuant to this
28 paragraph who is an affiliate of a distributor of new motor vehicles
29 licensed as such in any state prior to January 1, 2003, and
30 continuously thereafter, is exempt from the requirement that its
31 insurer or risk retention group satisfy the rating, surplus, and
32 paid-in capital requirements of paragraph (1). This exemption shall
33 apply only if the distributor sold or distributed at least 25,000 new
34 motor vehicles to licensed dealers in the preceding five years. For
35 the purpose of this paragraph, "affiliate" has the meaning set forth
36 in subdivision (a) of Section 1215.

37 (b) An insurance policy filed with the commissioner pursuant
38 to subdivision (a) shall state the name of the obligor. The policy
39 shall provide that all purchasers of vehicle service contracts shall
40 be entitled to satisfaction by the insurer of any and all obligations

1 arising under vehicle service contracts of the named obligor, upon
2 the existence of all of the following conditions and no others:

3 (1) The service contract obligor refuses or fails to satisfy an
4 obligation arising under the vehicle service contract within 60 days
5 of the date the purchaser submits proof of loss to the obligor.

6 (2) The purchaser provides written notice to the insurer that the
7 obligor has failed to comply with an obligation under the vehicle
8 service contract.

9 (3) The purchaser possesses a vehicle service contract sold after
10 the inception and prior to any cancellation of the insurance policy
11 required by subdivision (a), and the vehicle service contract recites
12 the name of the obligor that is insured by the policy as the obligor
13 of the service contract.

14 (c) An insurer's liability under a policy filed pursuant to
15 subdivision (a) shall not be negated by any failure of the seller, an
16 administrator, the obligor, or agents of any of these persons, to
17 report the issuance of a vehicle service contract or to remit moneys
18 to another person pursuant to a contractual agreement. The policy
19 must state that the insurer is deemed to have received the premium
20 for the policy upon payment by the purchaser for a vehicle service
21 contract insured by that policy.

22 (d) An obligor may have on file with the commissioner only
23 one active policy from one insurer at any time *unless the obligor*
24 *files with the commissioner annually a report certified as accurate*
25 *by an officer or director of the obligor that lists each of its insured*
26 *vehicle service contract programs and the corresponding insurance*
27 *policy under which each program is insured.*

28 (e) No policy cancellation by an insurer shall be valid unless a
29 notice of the intent to cancel the policy was filed with the
30 commissioner 30 days prior to the effective date of the cancellation,
31 or 10 days prior in the event that the cancellation is due to fraud,
32 material misrepresentation, or defalcation by the obligor or its
33 administrator, if any.

34 SEC. 8. No reimbursement is required by this act pursuant to
35 Section 6 of Article XIII B of the California Constitution because
36 the only costs that may be incurred by a local agency or school
37 district will be incurred because this act creates a new crime or
38 infraction, eliminates a crime or infraction, or changes the penalty
39 for a crime or infraction, within the meaning of Section 17556 of
40 the Government Code, or changes the definition of a crime within

1 the meaning of Section 6 of Article XIII B of the California
2 Constitution.

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